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ECONOMIC EXCHANGE UNDER ASYMMETRICAL OPTIONS: THE CHALLENGE OF PEACE WITH ISRAEL[*]

by

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Economic Exchange Under Asymmetrical Options: The Challenge of Peace With Israel

Atif Kubursi
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1.0 Introduction

In a comparative assessment of the global economy and the capacities of states and societies to adjust to its endemic changes the American historian, Paul Kennedy, observes that "more than any other developing region" the countries of the Middle East and North Africa are afflicted by the debilitating issues of wars and internal disorders as "[v]icious one-man dictatorships glare threateningly at arch- conservative, anti-democratic, feudal sheikdoms." In Kennedy's assessment, the Arab world remains least prepared to meet the challenges of the next century.

Equally pessimistic and critical of Arab chances in the next century is a 1995 World Bank study titled Global Economic Prospects and Developing Countries. It portrays a pessimistic and bleak outlook for economic growth and development in the Middle East and North Africa. During the 1980s, according to this study, the region's economic growth averaged less than one per cent with the world average being over three per cent. A Combination of population growth around three per cent, falling real oil revenues, dismal export performance, a terrible cost of two Gulf wars, Israel's vital challenge to the Arab East, several civil wars, and an unending wasteful expenditure on military procurement have coalesced to undermine any meaningful future economic prospects for the region.

While indeed the 1980's represent a lost decade for the Arabs and the early 1990's do not augur for much improvement, the real question is-- why has development remained so illusive in the Arab World? What are the basic explanatory factors of this abysmal slow growth? What accounts for the success of southeast Asians and many other developing regions that outperformed the Arabs? What is needed to reverse the negative sliding economic trends? Can a collective Arab development strategy contribute to a brighter economic future for the Arabs? Will peace with Israel bring prosperity to Arab economic future? Is the Euro-Mediterranean project a viable alternative? Why has Arab economic cooperation been so limited and disappointing? Where should the Arabs begin?

Meanwhile Israel has experienced a major economic boom in the early 1990's with real GDP growth topping 6% for most of the years between 1990 and 1995. Israeli per capita GDP is over US$13,619 and this larger than the combined per capita income of all its neighbouring Arab countries.

It is perhaps an understatement to suggest that there does not exist a level playing field between the Arabs and the Israelis. This is no where more evident than in the economic domain. These asymmetries are also reflected in the terms and conditions of the recent political and economic agreements concluded between the Israelis and Palestinians. These agreements typically reflect the vertical organization of power and options in existence in the region and the world. It would be difficult to believe that the asymmetrical economic conditions that define their economic positions would not influence the outcome of any liberalization of trade and other economic exchanges between them.

This paper begins with a detailed analysis of the economic success of Israel and Arab economic failures and the reasons why the two economies have such a marked record of economic performance. We then proceed to consider the "old" economic theories about the possible effects of economic exchange between poor and more advanced economies and the more recent developments in economic thinking on these issues. We will also consider in the process what economic liberalization of trade would mean when it is directed towards similar and equivalent economies, how and why these arrangement among the Arabs have not worked, what to expect from peace and normalization of economic relations with Israel and end up with an Arab economic strategy to deal with the Israeli economic challenges.

2.0 The Arab Economic Malaise

Collectively the Middle East and North Africa grew at less than one half of one percent per annum between 1980 and 1990, whereas the Third World grew at an average rate of 3.4 percent per year during the same period.

Severe and entrenched structural weaknesses in the Arab economy hamper its ability to adjust to global change, meet the challenges of "peace" and protect itself from adverse changes in the international economic environment. Over the 70's and 80's Arab economic "success" has masked many of these structural problems. They are now becoming more visible and detrimental for future economic performance.

The most fundamental problem afflicting the Arab economy is its heavy (if not exclusive) direct and/or indirect dependence on the rent from natural resources (oil). This dependence has propagated an "Arab Disease" along similar but more profound manifestations of the "Dutch Disease" that afflicted Holland in the wake of rising natural gas prices at the end of World war II.

The Arab Disease manifests itself in a number of dysfunctions and malaise that are increasingly constraining the Arab economies capacity to grow and prosper.

First, increased oil revenues denominated in US dollars raised the exchange values of most currencies in the region. The rapid appreciation of domestic currencies undermined the capacity of the Arabs to export manufacturing products and made them more dependent on imported food and products.

Second, oil incomes bouyed domestic demand without raising domestic supplies. Cost of production in the non-traded goods sectors rapidly increased compromising in the process the capacity of local industry and agriculture to compete in even the domestic markets with cheaper imports. Domestic markets were flooded with cheap and large volumes of imports that ultimately compromised the balance of payments of even the richest states.

Third, large and massive infusion of petrodollars in the local economies engendered unsustainable high consumption patterns that were almost totally divorced from high production. The combination of high demand and low production raised domestic prices and increased the dependence on imports. Inflation redistributed incomes away from those on fixed incomes and distorted local investment. Real estate speculation absorbed the largest share of private investment.

Fourth, the huge rent on oil also encouraged public investment in large projects that often were unnecessary and unproductive and ultimately straddled the domestic economy with large maintenance costs that were not paid for from increased production or productivity.

Fifth, the oil rent was skimmed by governments. Two serious consequences developed out of this phenomenon. Government bureaucracies were bloated with overlapping rings of rent seekers with little or no contribution to production. Perhaps more serious was the reversal of the traditional relationship between the rulers and the ruled. Oil rent secured a large and continuous source of income to the ruler. It also insulated the ruler from the ruled. Rulers do not have to depend on the ruled for their sustenance. Without taxation there is no representation. The insulation of the ruler from dependence on and accountability to the ruled weakened democratic forces and shielded Arab rulers from the strong trends and tendencies towards democracy observed in other parts of the world. In fact a perversed relationship was established between the ruled and rulers as a result of oil rents. The ruled are now dependent on the rulers for their income and jobs. When the rulers spend the domestic economies expand and prosper and when they tighten the strings on the public purse domestic economies suffocate and contract. There is a direct relationship between democracy and economic development. Democracy mobilizes people and talents and allows for rational public spending and scrutiny. In the absence of democracy it is not possible to instill a public discipline on spending and people become alienated from their work and economy.

Sixth, rent seeking weakens the economy by also divorcing income from production and productivity and exposes the domestic economies to the wide fluctuations of the world market for oil over which the Arabs had but little control.

While it may be convenient to argue that the Arab economic difficulties in the 1980's can be explained totally by falling oil prices, the truth lies elsewhere. The fact, however, that oil prices can affect so adversely all economic indicators of Arab performance is itself revealing. In this respect the heavy dependence on oil rents is symptomatic of general economic failure.

Seventh, the Arab economy today remains almost as undiversified as it were in the 1970's. Oil exports are still the exclusive economic engine of the region. Rentierism is a widespread phenomenon and is not restricted to the oil rich countries. There is now a "secondary dependence" on oil revenues throughout the region. Exports of manufactured renewable commodities and services contribute very modestly to the external sources of finance of all Arab countries.

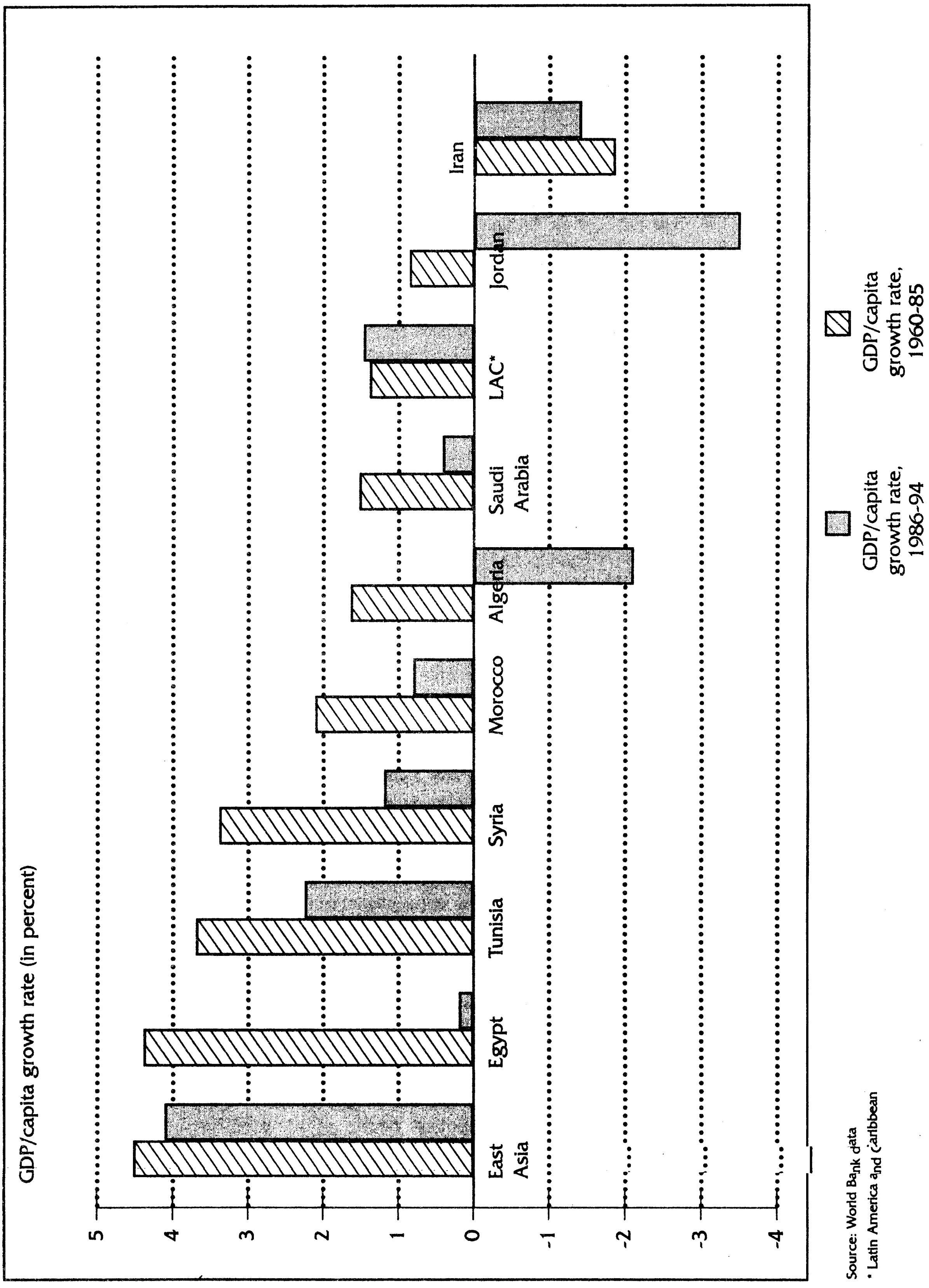
Non-oil producing Arab countries have exported their producers to the Gulf and have enjoyed the convenience of remittances to bother about developing domestic exports. Manufacturing activity outside oil is limited, disarticulated, traditional, inward looking, and technologically dependent on outside sources. Little or no technological capabilities are developed within the region. There is strong preference for "turn key" projects. Expenditures on research and development are modest if not totally inconspicuous. Regional cooperation is a political slogan without any real economic transactions (until today exclusive of oil Arab regional trade is only 4% of their total international trade and with oil it is less than 9%). Most Arab countries are linking to non-Arab economic centres with little or no concern for their Arab neighbours. External indebtedness is massive and is beginning to sap the energies of the region. The Arab region is still gambling on "sun set" industries and old Fordist and smoke stack manufacturing activities. There is little evidence of the new economy in the industrial structures of most Arab economies. Domestic savings are inadequate; they rarely finance investment. High and unproductive consumption habits have been staunchly ingrained in the operating systems of most Arab societies. Illiteracy is still excessively high particularly of females. Mean years of schooling have increased but remain far below other successful developing countries. Industrial policies are almost too stringent or absent and there is a tendency to adopt IMF peddled "policy fads" that are inappropriate for Arab development and values.

In short, dependency on the rent from oil has reduced Arab incentives to diversify their economies, develop alternative manufacturing capacities, promote export oriented industries, encourage domestic savings and anchor income on solid productivity grounds. Traditional economic activities and structures were maintained. Dependence on external sources of finance deepened and economic performance slipped. Although large oil revenues brought about significant improvements in health, education and infrastructure throughout the Arab world, they diminished the incentive to capitalize on these achievements. Arab economic performance in the 1980's is symptomatic of an "Arab Disease" that is more fundamentally damaging than the "Dutch Disease" that afflicted Holland in the 1940's following the discovery and commercialization of natural gas. Holland had fertile land, abundant water, a highly skilled labour force and a European infrastructure and market.

While the need for external sources of finance is urgent, the Palestinians must balance this urgency for finance against the negative and disastrous dependency on precarious international charity. They simply do not need to repeat the Arab experience in the 1970's and 1980's, and should try to avoid contacting this crippling Arab disease. The earlier they begin developing local and regional financing sources the better.

FIGURE ONE

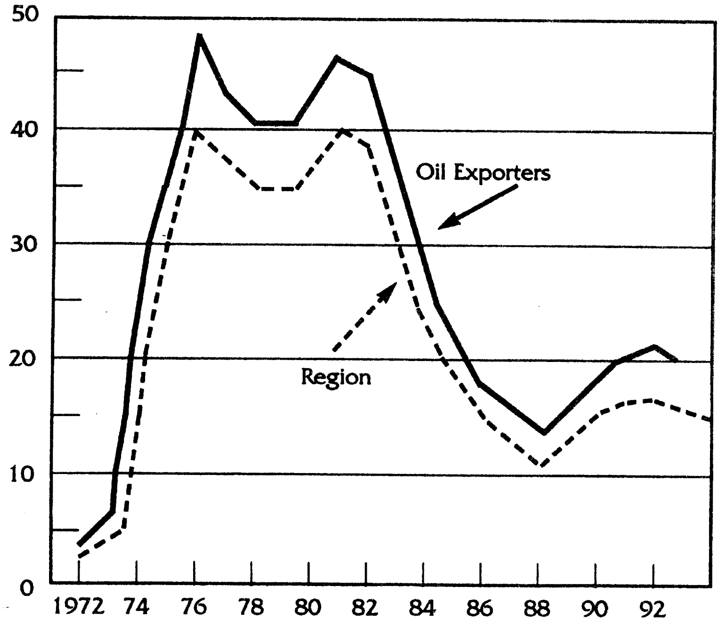
COMPARATIVE PER CAPITA GROWTH 1960-1994



Source: World Bank data
* Latin America and Caribbean

FIGURE TWO
PAST GROWTH CATALYSTS

OIL REVENUES

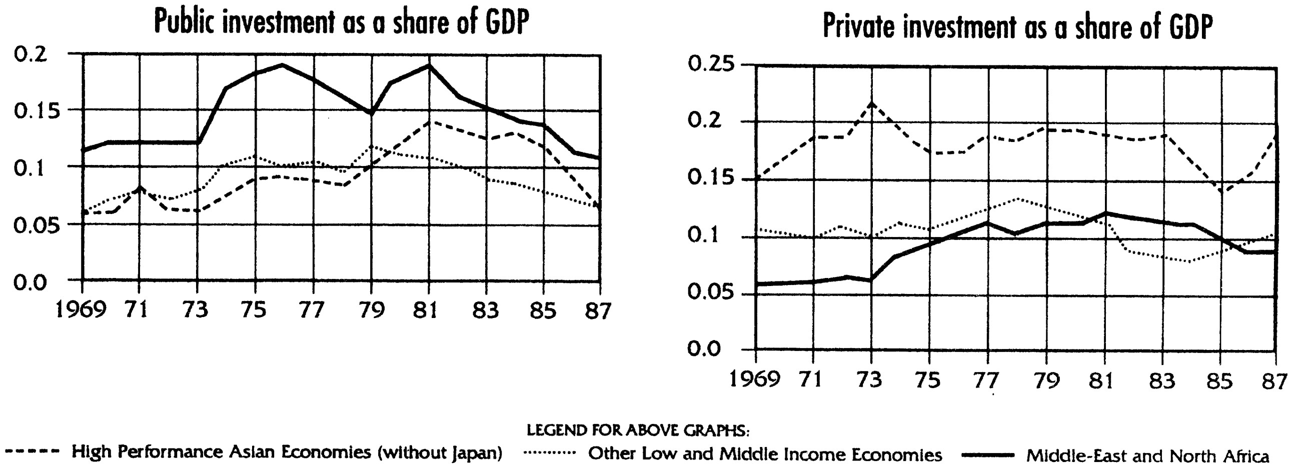


Export Revenues as a Share of Nominal GDP, 1970-93

Source: Dadush et. al. 1995.

Note: Figures represent a 3-year moving average of differences between actual and "counterfactual."

LARGE PUBLIC INVESTMENTS

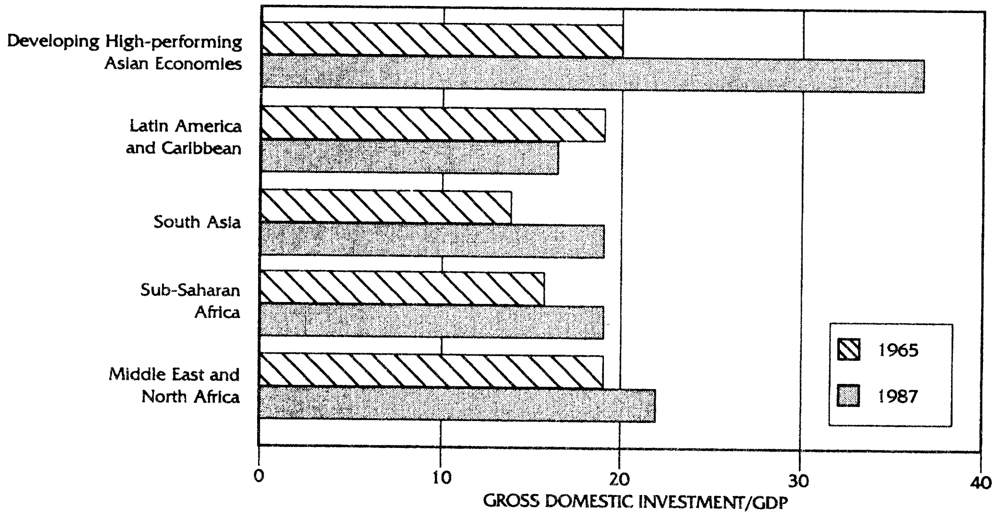


Public investment as a share of GDP

Private investment as a share of GDP

FIGURE THREE

INVESTMENT AS A PERCENTAGE OF GDP



SAVINGS AS A PERCENTAGE OF GDP

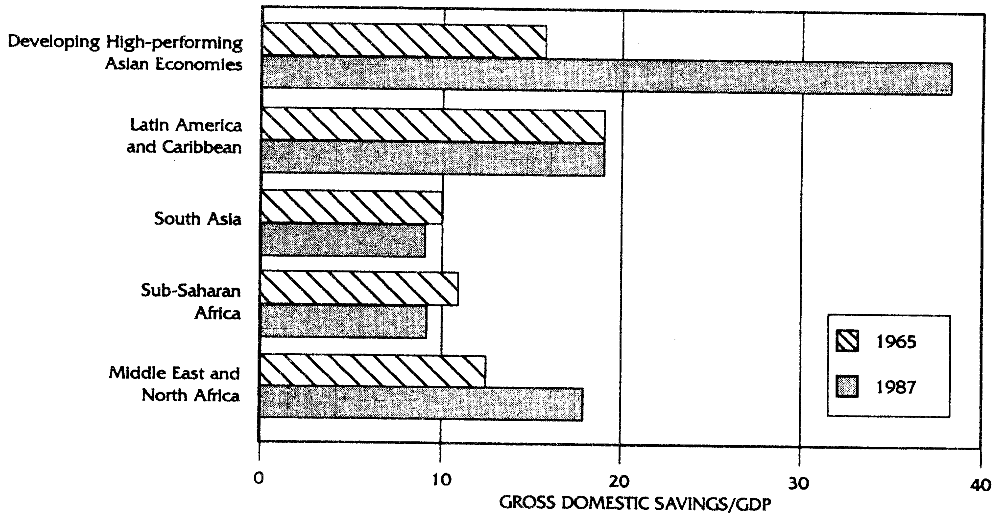


FIGURE FOUR

DIFFERENTIAL IN PER CAPITA INCOME GROWTH

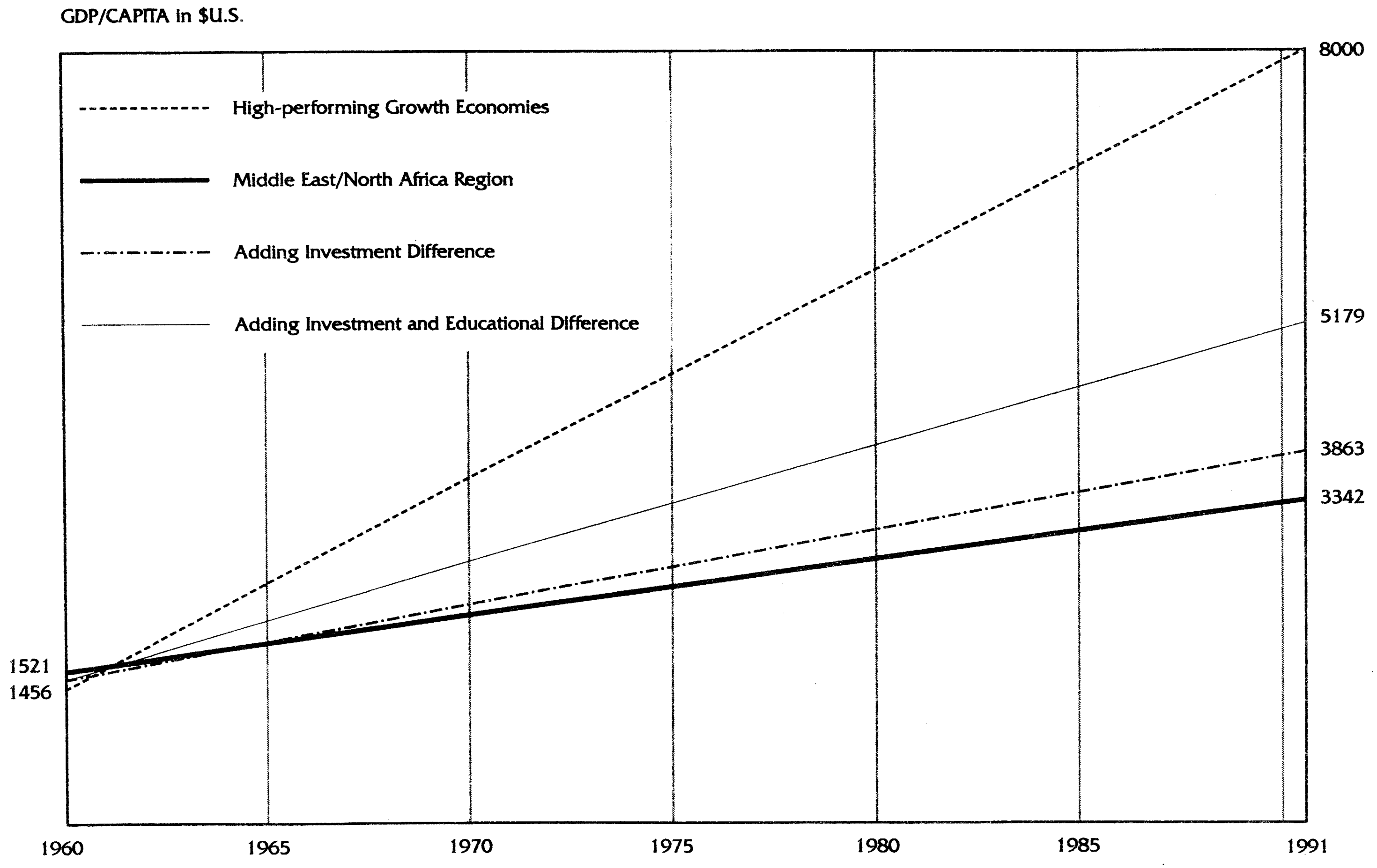


FIGURE FIVE
TRADE GROWTH BY PERIOD

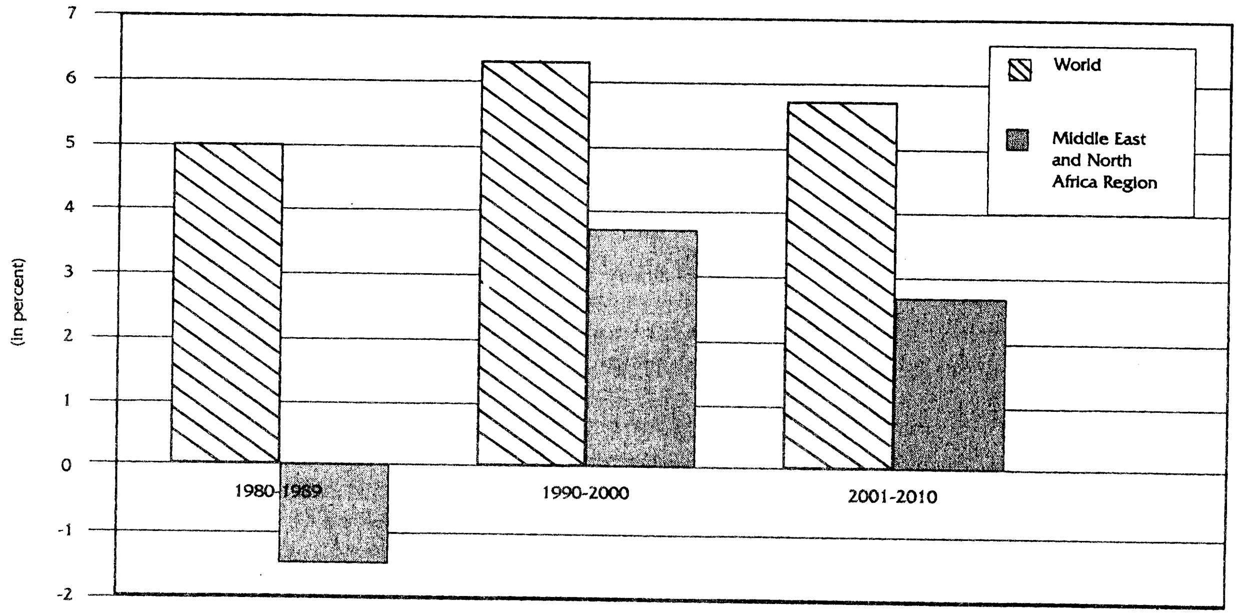


FIGURE SIX
INDEX OF PRICES RELATIVE TO WORLD PRICES

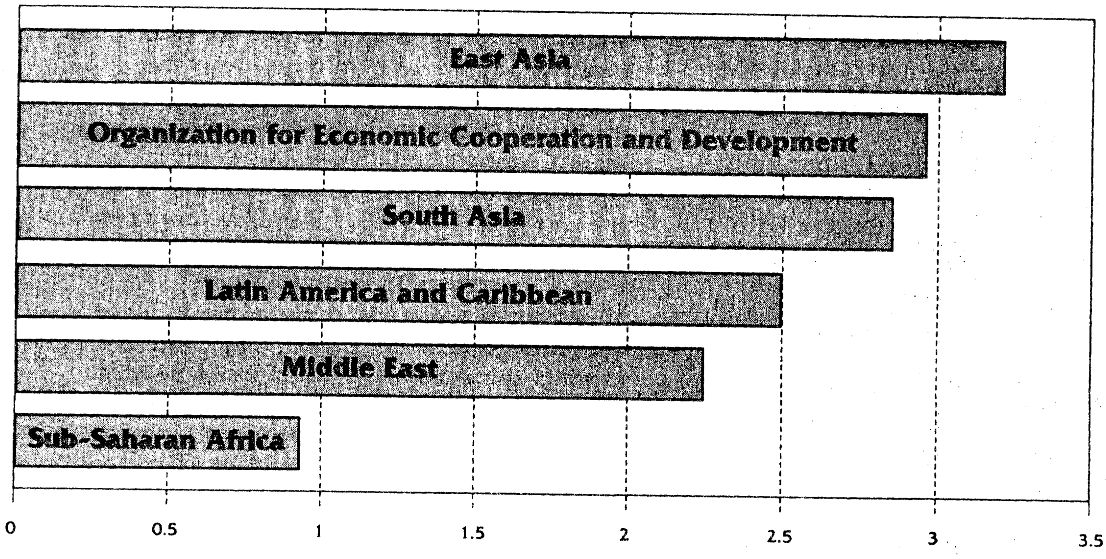


FIGURE SEVEN

PER CAPITA MANUFACTURING EXPORTS: MENA [GULF COOPERATION COUNCIL (GCC) & NON-GCC], AND EAST ASIA

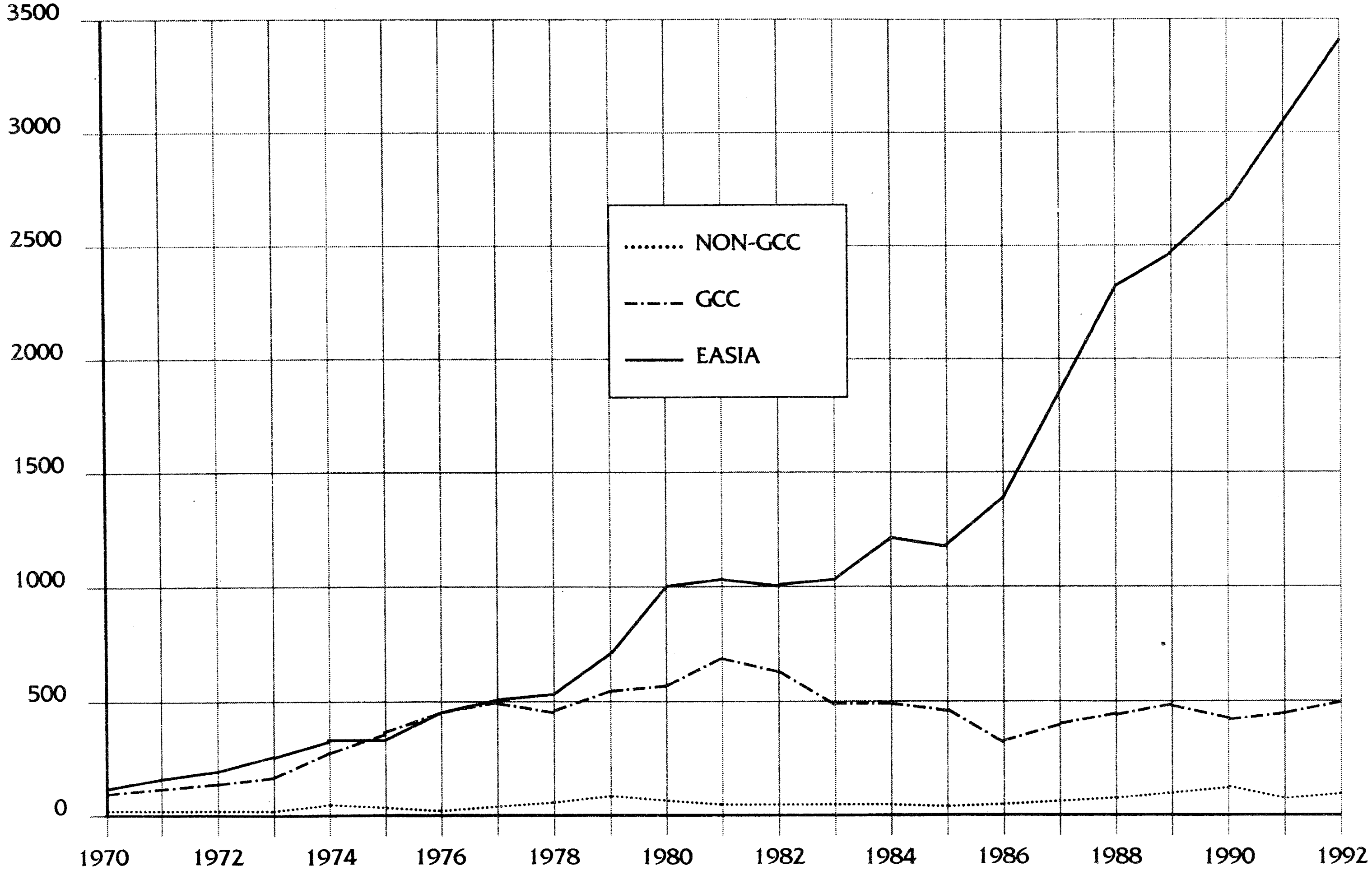


FIGURE EIGHT
AVERAGE TOTAL FACTOR PRODUCTIVITY 1960-90

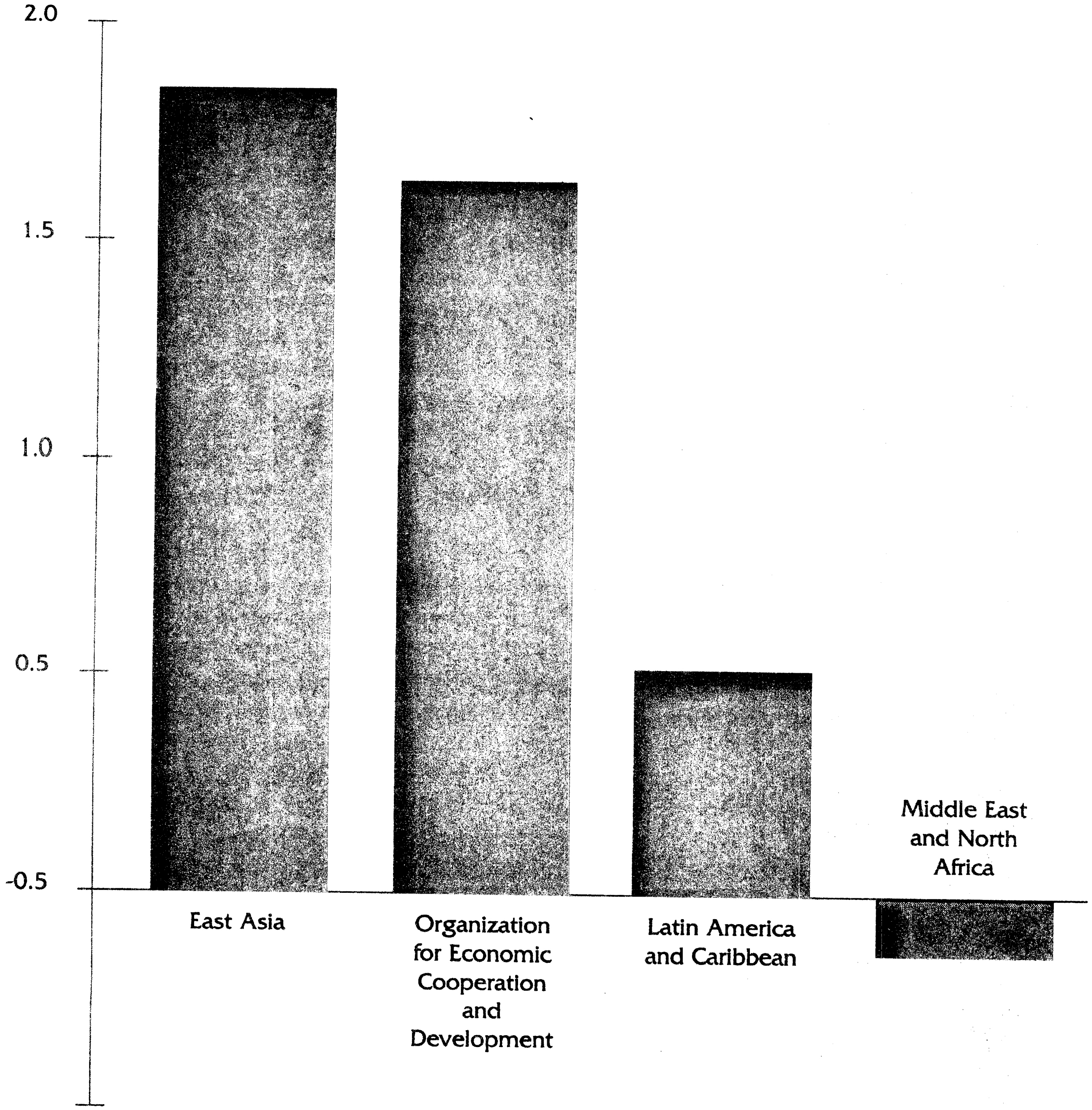
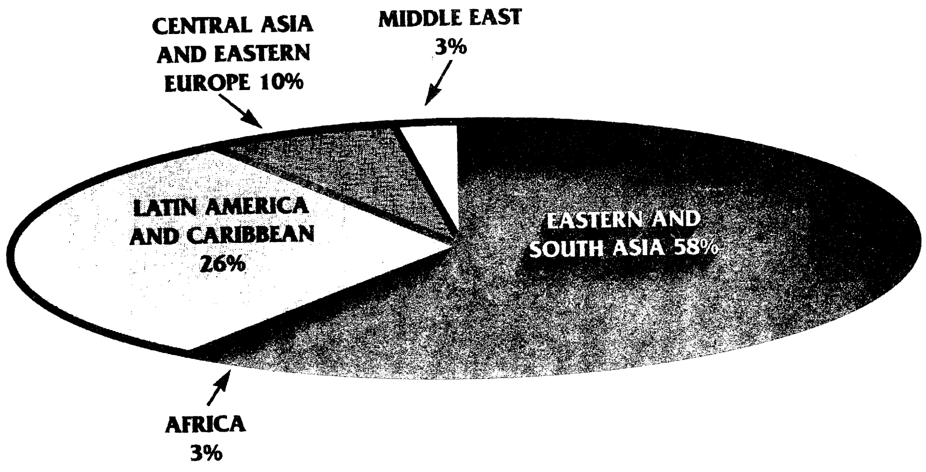
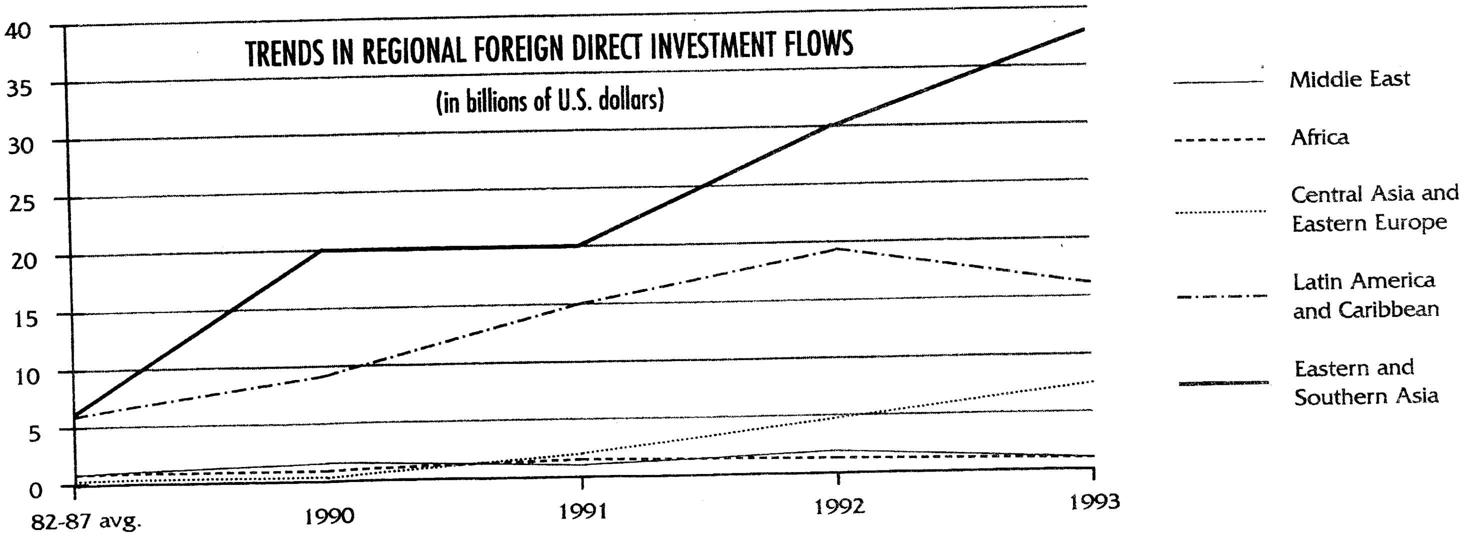


FIGURE NINE

FOREIGN DIRECT INVESTMENT IS LAGGING

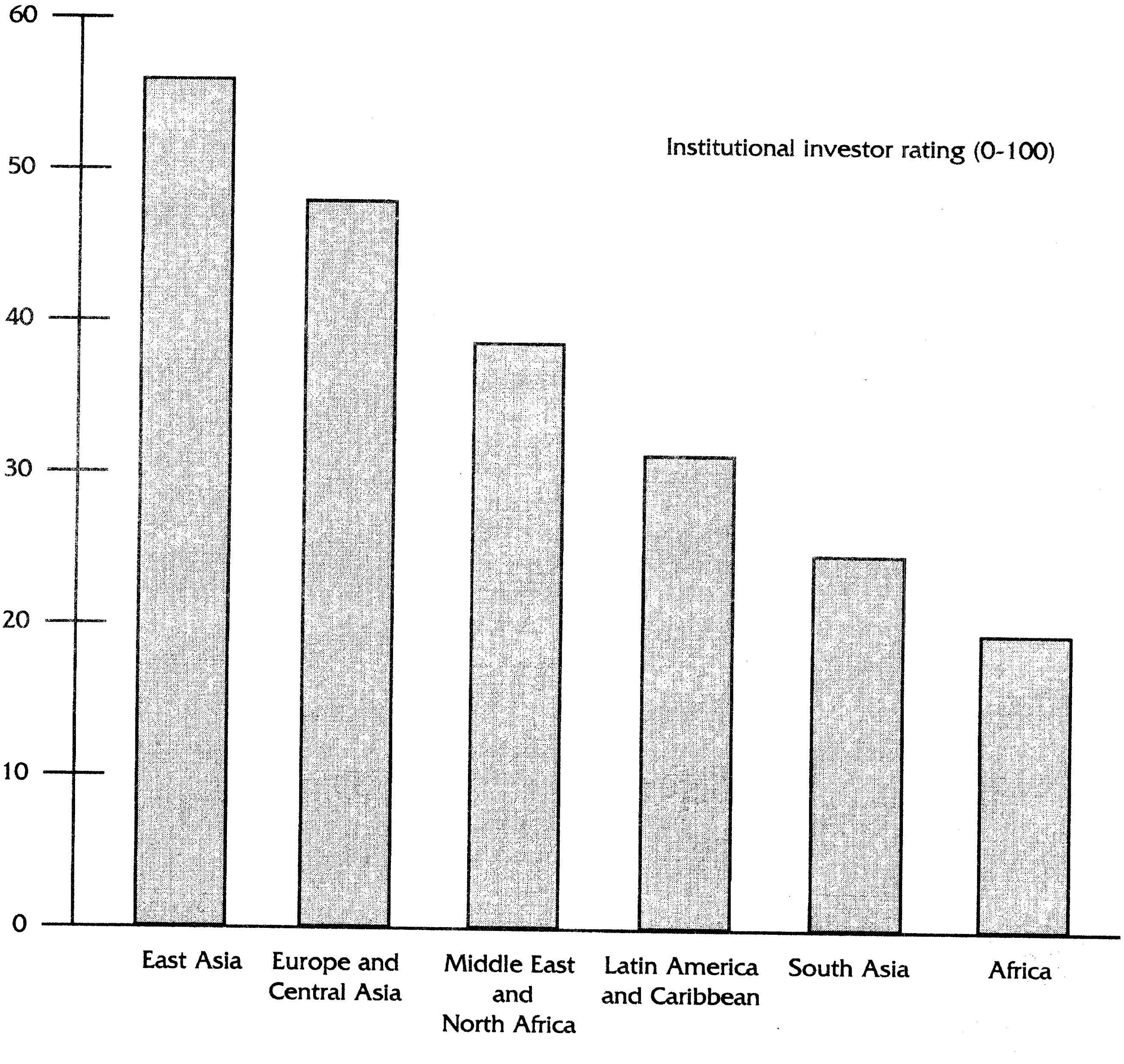
FOREIGN DIRECT INVESTMENT INFLOWS IN THE DEVELOPING WORLD - 1993




TRENDS IN REGIONAL FOREIGN DIRECT INVESTMENT FLOWS

(in billions of U.S. dollars)

FIGURE TEN
INVESTOR ATTITUDE RATING BY REGION



Note: Higher the number, higher the rating

3.0 Israeli Economic Success

By way of contrast, the Israeli economy is experiencing unprecedented rates of real growth. Actually as is clear from Figure 11 the rate of growth of real GDP is almost twice as high in the 1990s than it were in the 1980s. The post Oslo real rates are exceptionally high.

The marked changes in the Israeli economy pertain to a number of fundamental factors. Among the most important factors is the rate of Gross Fixed Capital Formation. First, Israel typically had a high investment ratio in GDP, but this rate slipped to %16.7 in 1987. In 1991, it climbed abruptly to 24% of GDP despite the fact that GDP was rising at very fast rates.

Second, Israel has suffered from high inflation rates since its inception. Double or triple digit inflation rates were typical in the 1970s and early 1980s. Israel succeeded in lowering this rate before Oslo to the 20% mark, but real declines did not happen until the year 1991.

Third, Israeli exports were rising at very slow rates in the late 1980s. Their rate of growth averaged less than 3% per year between 1987 and 1990. This rate of growth actually fell down between 1990 and 1991. Subsequently these rates grew very fast at rates that exceeded 15% in 1994.

Fourth, Israel has successfully re-arranged its production and export structures in the 1980s. The share of agricultural exports dropped from a high of 10.2% in 1980 to less than 3.8% in 1990. Textiles also lost market share in total exports falling from 8.3% to 6.1% during the same period. But the most stunning change is in the share of metal manufacturing whose share climbed from 21.9% to 36.7%. This category captures all sorts of heavy and sophisticated machinery and products.

While indeed real economic factors and policies had a lot to do with the transformation of the Israeli economy, it is inconceivable that Israel could have realized all the economic gains in exports and growth without the advantages it realized on the expectation and promise of peace.

4.0 Economic Theory and Free Trade Among Unequal Partners

Economic theory suggests that in equilibrium, under specified conditions, the long term outcome of exchange is that factor prices (advantage) are equalized throughout the world: the less skilled workers in poor countries will be paid the same wages as his or her counterpart in the advanced countries; and similarly for the skilled workers.

But does factor price equalization (appropriately qualified to fit an n-factor/n-good world capture economic reality? For years, many trade theorists rejected equal advantages from trade and factor equalization as a description of the world. The wide, and in some cases increasing, variation in pay levels within and among contrives seemed to make it a textbook proposition of little relevance. (For an exception to this point see Krueger, 1968). Reflecting this view, in the recent debate Bhagwati and Dehejia (1994) have enumerated some of the "extraordinary demanding" assumptions needed to establish factor price equalizations and even the simpler propositions about the gains from trade. These Include:

Table 1 Israeli Gross Domestic Product (GDP), 1980-94

YEAR	GDP (MILLIONS OF CURRENT NEW SHEKELS)	GDP AT 1990 PRICES (MILLIONS OF SHEKELS)	REAL GDP GROWTH	GDP(MILLIONS OF US$)	GDP PER CAPITA (US$)
1980	111.612	74,756	3.23%	21,780.926	5,613.64
1981	265.148	78,131	4.51%	23,258.596	5,888.25
1982	596.306	79,154	1.31%	24,539.342	6,089.17
1983	1,542.000	81,165	2.54%	27,437.722	6,675.84
1984	7,636.000	82,900	2.14%	26,043.656	6,260.49
1985	28,454.000	86,222	4.01%	24,138.107	5,706.41
1986	44,563.000	89,789	4.14%	29,952.279	6,965.65
1987	56,906.000	95,306	6.14%	35,686.693	8,166.29
1988	70,225.000	98,246	3.08%	43,920.821	9,892.08
1989	85,642.000	98,483	0.24%	44,689.000	9,886.95
1990	105,216.000	105,216	6.84%	52,185.299	11,198.56
1991	135,635.000	111,787	6.25%	59,512.527	12,022.73
1992	161,279.000	119,157	6.59%	65,584.563	12,809.49
1993	184,078.000	123,824	3.92%	65,042.931	12,365.58
1994	221,456.000	131,833	6.47%	73,546.544	13,619.73

Source: International Monetary Fund (1996), *International Financial Statistics Yearbook,* Washington: IMF, 448-49.

FIG. 11: ISRAELI REAL GDP GROWTH 1980-94

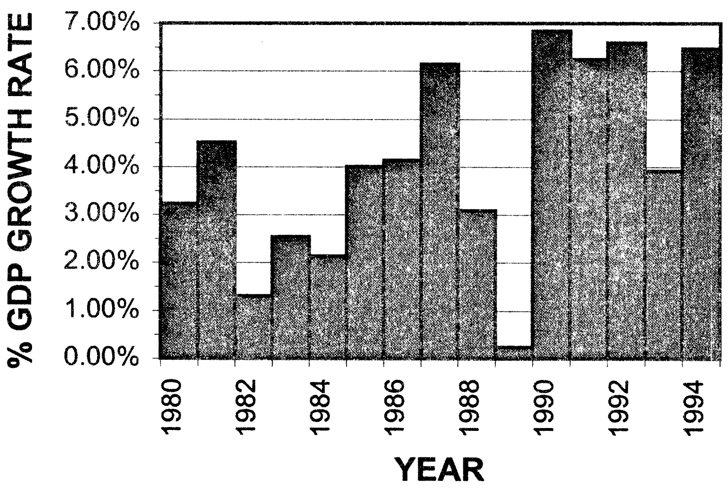


Table 2 Israeli Gross Fixed Capital Formation (GFCF), 1980-94

YEAR	GFCF (MILLIONS OF CURRENT SHEKELS)	GFCF AS % OF GDP
1980	24.583	22.03%
1981	59.002	22.25%
1982	136.006	22.81%
1983	360	23.35%
1984	1,568	20.53%
1985	5,331	18.74%
1986	7,962	17.87%
1987	11,105	19.51%
1988	12,610	17.96%
1989	14,299	16.70%
1990	20,092	19.10%
1991	32,575	24.02%
1992	37,580	23.30%
1993	41,615	22.61%
1994	51,027	23.04%

Source: International Monetary Fund (1996), *International Financial Statistics*, Washington: IMF, 448-9.

FIG. 12: GROSS FIXED CAPITAL FORMATION AS A PERCENTAGE OF GDP

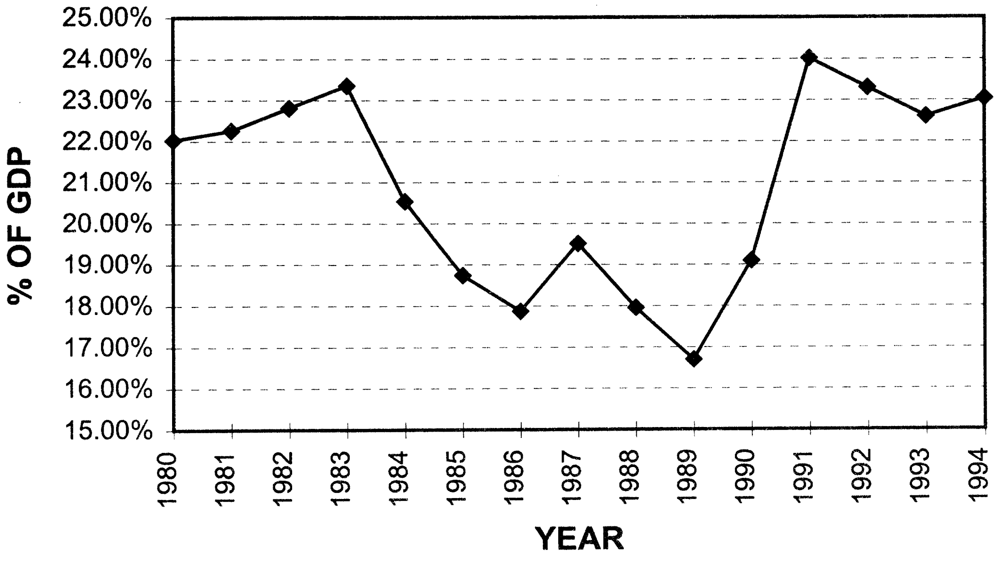


Table 3 Israeli Unemployment Rates, 1980-94

YEAR	UNEMPLOYMENT RATE
1980	4.80%
1981	5.10%
1982	5.00%
1983	4.50%
1984	5.90%
1985	6.70%
1986	7.10%
1987	6.10%
1988	6.40%
1989	8.90%
1990	9.60%
1991	**10.60%**
1992	**11.20%**
1993	**10.00%**
1994	**7.80%**

Source: *United Nations' Statistical Yearbook 41st ed.*, 1994.

FIG. 13: UNEMPLOYMENT RATE 1980-94

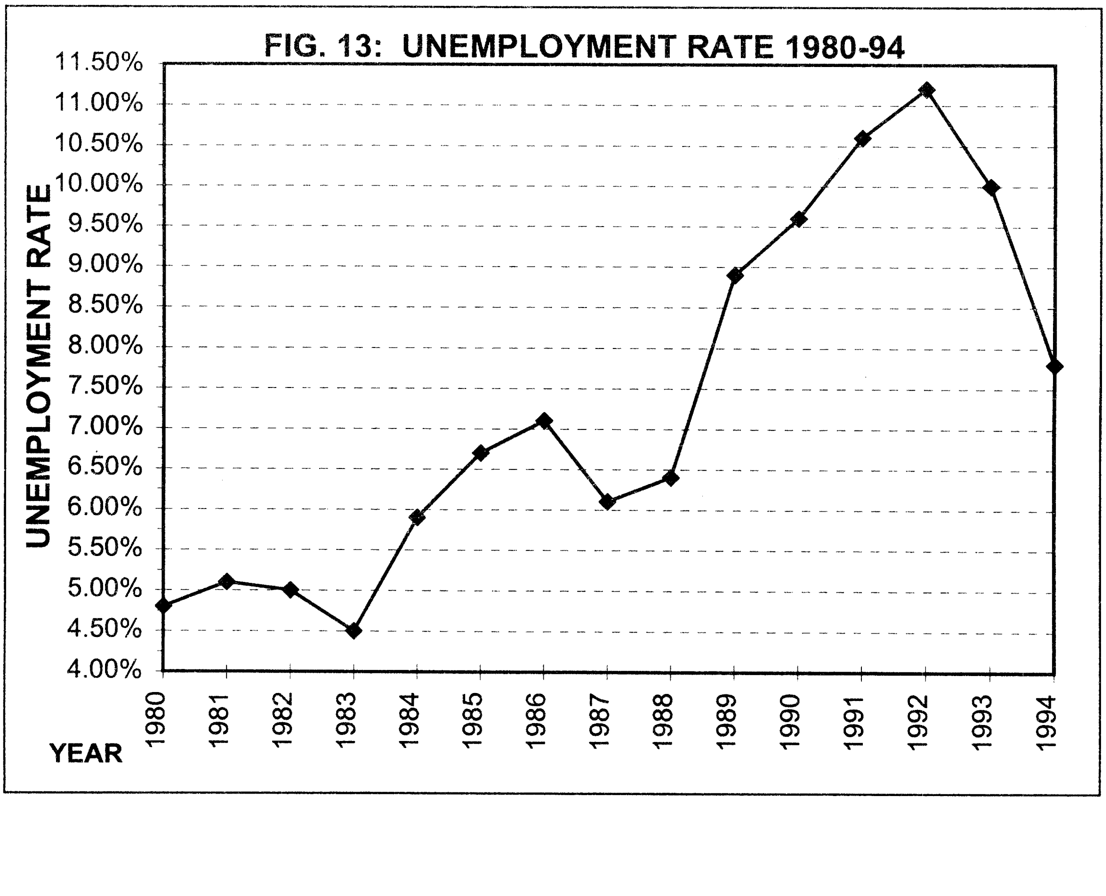


Table 4 Israeli Price Deflators

YEAR	CPI (1980=100)	GDP DEFLATOR (1990=100)	% CHANGE IN CPI	INFLATION (BASED ON GDP DEFLATOR)
1982	0.7	1	157.14%	100.00%
1983	1.8	2	372.22%	350.00%
1984	8.5	9	304.71%	266.67%
1985	34.4	33	47.97%	51.52%
1986	50.9	50	19.84%	20.00%
1987	61.0	60	16.39%	18.33%
1988	71.0	71	20.14%	21.13%
1989	85.3	86	17.23%	16.28%
1990	100.0	100	19.00%	21.00%
1991	119.0	121	11.93%	11.57%
1992	133.2	135	10.96%	10.37%
1993	147.8	149	12.31%	12.75%
1994	166.0	168		

Source: *United Nations' Statistical Index 41st ed.*, 1994.

FIG. 14: ISRAELI INFLATION RATES, 1982-93

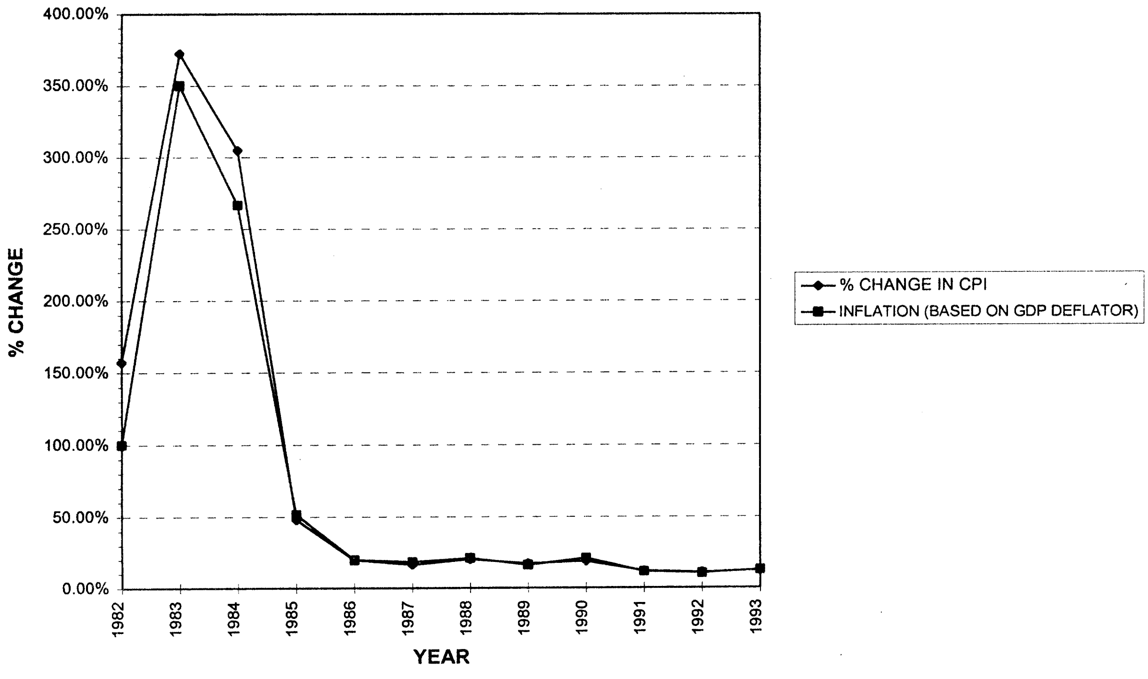


FIG. 15: ISRAELI INFLATION RATES, 1986-93

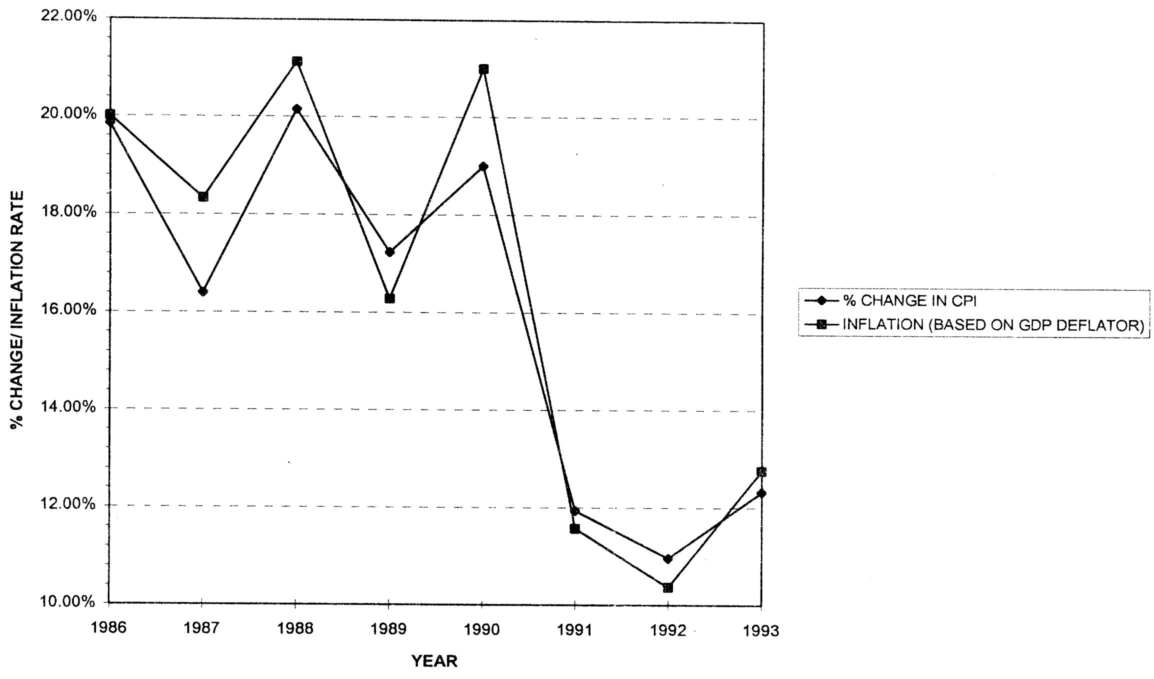


Table 5 Direct Investment in Real Private Economy

YEAR	DIR. INV. IN ECON. (MILLIONS OF $US)
1980	51
1981	114
1982	51
1983	88
1984	53
1985	99
1986	137
1987	233
1988	235
1989	125
1990	101
1991	351
1992	539
1993	580
1994	421
1995	1637

Source: International Monetary Fund (1996), *International Financial Statistics*, Washington: IMF, 448-9.

FIG. 16: DIRECT INVESTMENT IN ECONOMY, 1980-94

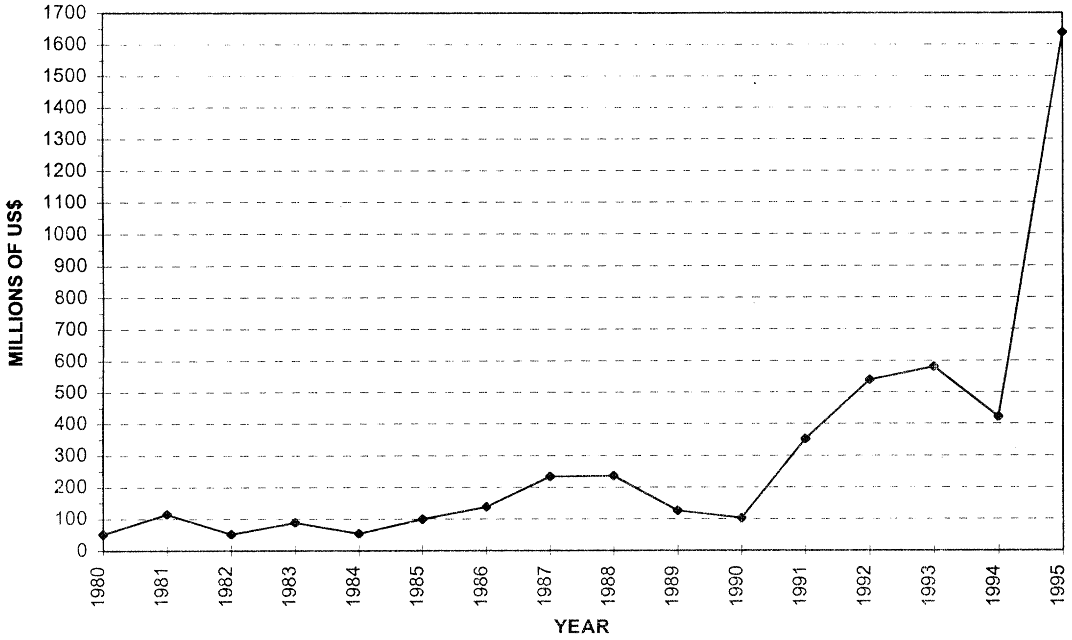


Table 6 Israeli Volume of Exports, 1980-95

YEAR	VOLUME OF EXPORTS (1990=100)	GROWTH IN VOLUME OF EXPORTS
1980	56.9	9.21%
1981	60.3	5.98%
1982	59.2	-1.82%
1983	59.8	1.01%
1984	68.9	15.22%
1985	75.1	9.00%
1986	83.2	10.79%
1987	92.2	10.82%
1988	95.2	3.25%
1989	99.5	4.52%
1990	100.0	0.50%
1991	97.9	-2.10%
1992	107.1	9.40%
1993	120.8	12.79%
1994	139.7	15.65%
1995	150.3	7.59%

Source: International Monetary Fund (1996), *International Financial Statistics*, Washington: IMF, 448-9.

FIG. 17: GROWTH IN VOLUME OF EXPORTS, 1980-95

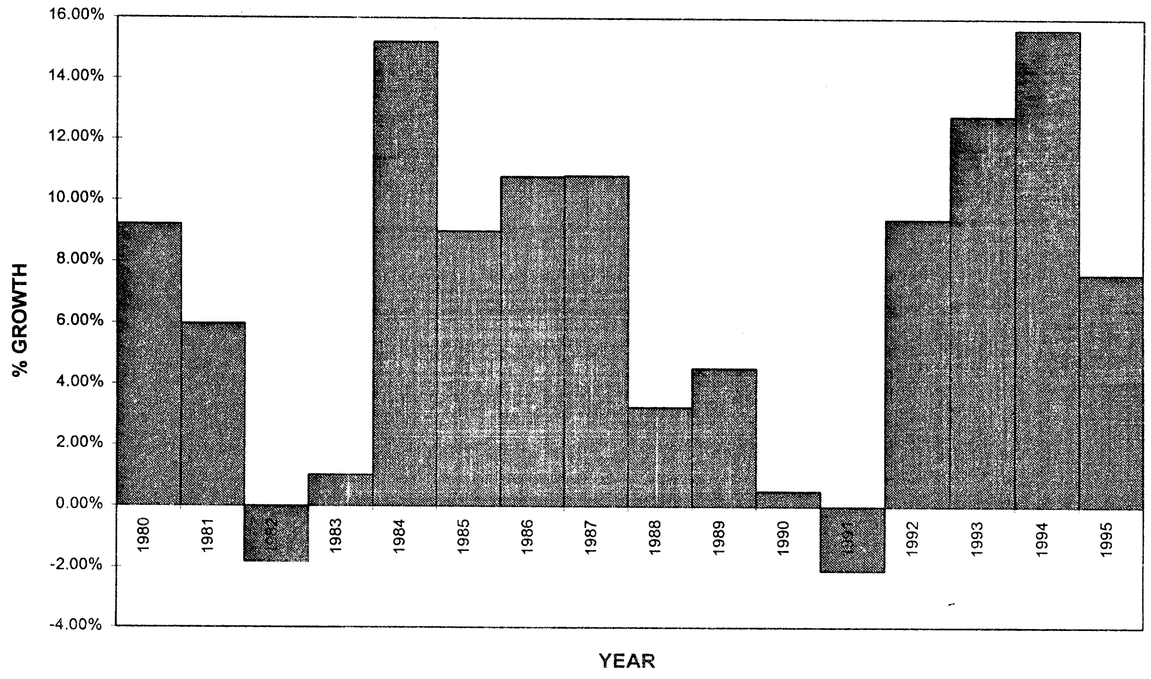


FIG. 18: COMPOSITION OF ISRAELI EXPORTS, 1980

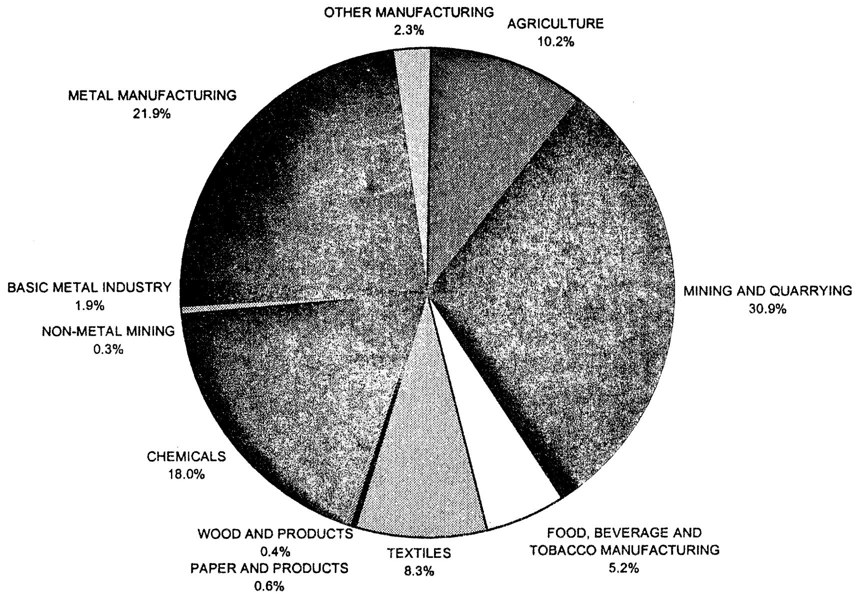
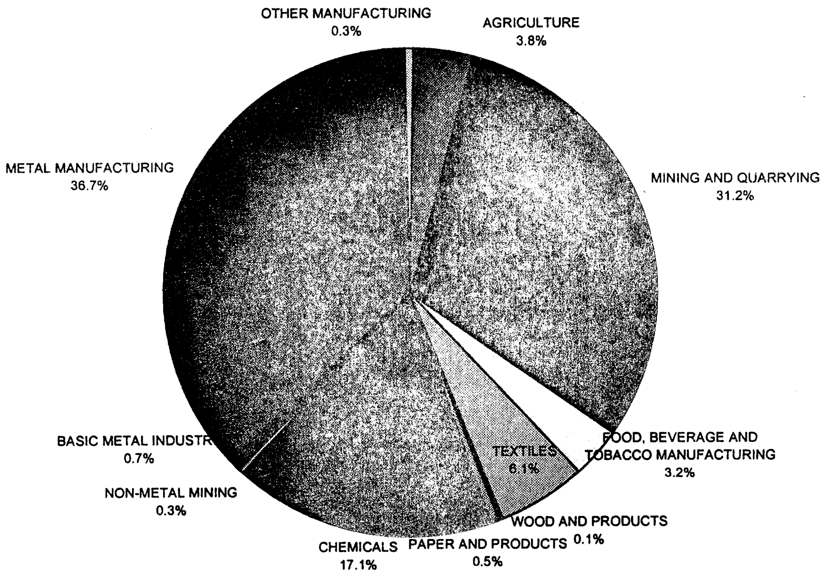


FIG. 19: COMPOSITION OF ISRAELI EXPORTS, 1994



- Identical Technology and that the same production functions are in existence in all countries.
- Identical Tastes
- Similar ranking of sectors by skilled to unskilled and labour to capital intensity at all prices
- Absence of any economies of scale
- That the countries are incompletely specialized, i.e., that they produce the full set of traded goods.

Norman and Venables (1993) stress that in a Hecksher-Ohlin model where cost of trade are non-negligible, goods trade alone does not equalize factor prices; flows of capital and labour would also be needed.

There are many trade theorists today that believe that trade itself is leading to global inequality and that trade is exacerbating factor price diversions.

5.0 Arab Economic Cooperation: Lessons from the Past

Today the Arabs are wrestling with some of the greatest economic challenges they have ever faced. The future of the Arab economy will depend on the choices made today. Ironically, these choices are being made and will be made under duress with little or no regard for their implications for the future. While there is a critical need for the establishment of broad-based agreement among the Arabs on what it takes to succeed in the global economy and a desperate call for a common sense of purpose and a shared vision that will help them improve productivity, competitiveness in the world, there are centrifugal forces woeing them apart and tearing at the fundamental linkages that tie them together.

Each Arab country is taking independent initiatives to deal with its future but while individual state action is necessary it is not sufficient; it will always be small and insignificant in today's global world markets and giant multinationals. This is all the more important in view of western and Israeli designs for shaping the region's future. These designs are predicated on attracting each Arab country separately into their folds. The Arabs can no longer escape or postpone choosing their future economic course from among the current alternatives before them. The choices are real and limited. The competition is basically among three contenders-- the American/Israeli New Middle East project, the European (primarily France) Mediterranean project and a new and invigorated independent Arab collective action?

The past record of Arab economic cooperation is dismal. The question is whether the severity of the challenges and the new regional projects will bring a new life and shape to old Arab aspirations, or add to Arab fragmentation, dependency, humiliation and instability?

The plan of this section of the paper is to begin with a brief examination of old Arab cooperation/integration projects and why they have failed. Then to consider lessons from other regional cooperation efforts before evaluating the new projects and what they bode for the Arabs with special emphasis on the Palestinian and Israeli economic agreements as a case study of what other Arab countries can expect from the New Middle East project. The final section ends with some suggestions for an alternative Arab strategy after Oslo.

There is overwhelming international evidence that countries that opted for export promotion and open trade with their partners have achieved higher economic growth rates than those that continue to protect their domestic markets and emphasize import substitution policies. But there is little evidence why some countries were successful in exporting in the first place and why others failed to penetrate the world markets despite serious efforts and dogged determination to do so.

Most of the Arab economies are simply too small to be self-sufficient or self-sustaining. Individually, very few of them have sufficient economic sizes for rapid industrialization or diversified growth. It follows that Arab regional trade arrangements would be a natural response to these limitations. With cooperation and freer trade among trading partners would come mutual gains that result from the internal and external economies of larger markets, from augmented bargaining strengths, from the pooling of resources, from inter and intra industry specialization, and from freer mobility of resources.

Indeed, the recent history of the Arab World is rife with examples of attempts at Arab economic and/or political cooperation or integration. Unfortunately, most of these attempts were short lived, resulted in limited results and ended up in disappointments. Syria and Lebanon had a full fledged custom union that operated smoothly throughout the French mandate, but was dissolved in 1950. The British had in effect a less extensive custom union over their mandatory area that included Palestine, Jordan and Iraq that elapsed with the end of British rule in Palestine in 1948. The United Arab Republic (UAR), unified Egypt and Syria for less than three years between 1958 and 1961, was the first such attempt by two independent Arab governments but collapsed under the weight of a hostile coup d'etat in Syria. The UAR opened the way, however, to many more such attempts whose fate, however, was not more promising. Among them were, the frequent efforts of president Qaddafi to unite Libya with Egypt, with Sudan and with the Maghreb countries and most recently, the formation of the Gulf Cooperation Council in 1980, The Maghreb Cooperation Council in February 1989, and the Arab East Cooperation Council that included Iraq, Jordan and Yemen in March 1989. These attempts held the prospects for more realistic achievements and survival. In actual fact, President Qaddafi's attempts failed, the Maghreb Cooperation Council is dormant and the Arab East Cooperation Council is practically dead. Only the Gulf Cooperation Council is still alive, albeit with some serious problems and challenges.

More serious and enduring but no more successful perhaps was the project that began in 1953 with the promulgation of the Arab Joint Defence and Economic Cooperation Treaty that gave rise to the Agreement on Arab Economic Unity that was signed in 1957, came into effect in 1960 and gave birth to the Arab Common Market in 1964. The Agreement, which led to the creation of some sixty pan-Arab or inter-Arab organizations, had otherwise only limited real economic results. Far reaching economic cooperation or integration remained principally more declaratory than real. Arab leaders and important segments in the Arab state system paid lip-service to its virtues and necessity but blocked any real steps to its realization, preferring instead to shelter their domestic economies and power spheres from any real or perceived "encroachments" by neighbours and brothers.

The absence of genuine democracy in most countries of the Arab World proved to be a real hampering factor for meaningful Arab cooperation. The lack of democratic principles and institutions militated against the ability of masses and majorities that believed and demanded cooperation from being able to exert sufficient pressure on their rulers for accommodating their aspirations. It also meant that whatever agreements were reached about joint activities and programs remained agreements among leaders and did not involve the participation and/or approval of the people.

With Israel separating physically the Arabs of Africa from those in Western Asia, the effort to link and expand the Arab economic space suffered yet another set back. But Israel's real negative impact on Arab cooperation came with the signing of the Camp David Accords in 1979 which dissociated Egypt from the rest of the Arab cooperative efforts until 1990. The Camp David Accords gave birth to the new Oslo Agreements in 1993 and 1995, the Israel-PLO Protocol on Economic Relations signed in Paris in April 1994, and the Peace Treaty between Jordan and Israel in 1994. Separately or in combination, these treaties are tearing the Arab World apart, reorienting the Palestinians and Jordanians away from their traditional trading partners and brethems and blocking the chances of wider Arab cooperative efforts.

There are also, to be sure, some basic economic reasons why Arab economic cooperation efforts in the past did not bear the fruits they were expected to. First, many of the Arab economies are characterized by similar patterns of specialization. This reduced the opportunities for avoiding competition among them. Second, most of the projects for wider Arab cooperation were premised on maximizing the effects of "trade diversion" from the rest of the world with little or no concern for "trade creation". Once the beneficial effects of trade diversion were realized, the benefits from cooperation were exhausted. Not surprisingly, most of these efforts did not last long. Furthermore, in a way, Arab efforts towards cooperation were marred by an implicit state agenda for broadening its planning sphere in the economy and for extending the boundaries of production for import substitution. In these circumstances politics inevitably intervened. Partners strived to avoid the costs and pains of adjustments that these agreements often entailed (Lawrence, 1995). They were typically unwilling to lose domestic industries and activities to other members of the agreement even when there were offsetting gains elsewhere from it. Allocation and deployment decisions became political decisions that were far removed from market realities and dictates (Langhammer, 1992). When one country was given the right to a particular industry or activity, other members demanded compensation, with the result that short-term distributional considerations dominated medium and long-term efficiency considerations.

Despite the many disappointments and failures of the past, a large Arab intellectual constituency remains wedded to the project of wider Arab economic cooperation and collective action . A sample of this literature would include the works of Al Dajani (1966), Hujayr (1967), Al-Ghandur (1970), Nawfal (1971), Al-Sakban (1975), Awwad (1977), Al-Mundhiri (1978), Abd Al-Fadil (1981), Duwaydar (1982) and Farraj (1986).) The failures of past Arab attempts at cooperation and/or integration are only matched by a massive literature, that keeps pouring in, on the advisability and necessity of Arab collective action. The old emotional appeals are giving in to a more serious and sombre literature analysing failures and pointing to the dangers of individual action in the face of the new challenges posed by new schemes and projects designed for dismantling the region's collective will to work together. One common theme runs across most of the new contributions--the Arabs are better advised to work together and solidify their common interests before they join any new arrangements (see Al-Imam (1994), Al-Khawli (1994), Abd Al-Fadil (1995), Sayyegh (1995), Kubursi (1995) and Chalabi (1995).)

The dialectics of failures on the ground and high expectations for and strong emotional commitments to Arab cooperation are raising doubts about and strong resistance to alternative projects that include Israel and/or wider Mediterranean involvement before the Arabs can come together as a work-able economic collective. This is taking palce at precisely the same time that agreement after agreement on the ground are being promulgated that set the Arabs away from one another--Paris Protocol between Israel and the Palestinians, North Africa and the European Market, etc. These contradictions are also spawning some highly critical evaluations of old indigenous options and wider realization that the old ways have not worked and that there are some serious economic and political issues that the Arabs need to address at a non-emotional level. The general feeling among Arab economists is that contending alternatives must be evaluated thoroughly and critically against the lessons learnt from the experiences and achievements of other regional cooperation projects in the rest of the world, and that regional Arab economic groupings must be retried first.

Below I present a brief discussion of the experiences of other regional cooperation efforts in the hope that such a brief consideration will shed some light on what the Arabs can realistically expect from these projects and what they can count on to work for them and what does not.

7.0 Lessons Others Learnt About Regional Cooperation?

Preferential trading arrangements (PTAs) do not have a good economic track record (Lawrence, 1994). They are typically greeted with justifiable criticisms in developing countries where they have particularly failed in the 1950's and 1960's to spur growth and equitable sharing of benefits as they were expected to or hoped they would. On the other hand, they have worked very well for the Europeans both in the EEC and in the EFTA. The lesson drawn from this is that these arrangements are suitable only for developed countries at the same stage of development and with similar factor endowments and equal access to technology. Developing countries, by way of contrast, are typically at different stages of development, have varying resource endowments and technical skills and are as such not in a position to benefit much from them (Yamazawa, 1992).

Differences of opinion abound, however, as to why these arrangements have failed in developing countries. Lawrence (1995) attributes their failure in developing countries to the motivation of the participants and not to differences in resource endowments or stages of development. He argued that the failure arose out of the pursuit of protectionist blocs and from the extension of import substitution policies to the bloc, while success was based on reinforced internal and external liberalization. He strongly advances the proposition that unless participating countries are willing to allow their economies to be heavily influenced by market forces, the arrangements would fail. Amsden, Yamazawa and others feel that the issue here is not about subordinating the economy to market forces as much as the ability to expand the market and overcome barriers to development and to wider access to richer markets. Liberalization seems to work best when an external market exists which allows the exporting country to expand and take advantage of the new economies of scale and scope.

While it is true that developing countries emphasized "trade diversion" and failed to " promote "trade creation", it is a contentious question whether or not their failure to create new trade among themselves reflects developmental barriers rather than being the outcome of market failures. There are many regions within the most advanced economies of the world that rely heavily on market forces and where free mobility of factors of production is assured but where growth remains a problem (e.g., southern Italy, Appalachia in the USA, and the maritime provinces in Canada). If subordination to market forces is sufficient, these areas should have no problem.

Equally important is the definition of whether the benefits in question are in terms of static or dynamic efficiency. It is the power to innovate, to access and adapt new technologies and attract foreign investment that is at the heart of the problem here. PTA's by themselves cannot spur the entrepreneurial spirit neither can liberalization? The issues are more complex than is acceded by the debaters. There are new economic models (Endogenous Growth theory and Chaos theory) that emphasize different factors than those invoked by free traders and import substitutionists. The EEC countries and Mercosur (involving Argentina, Brazil, Paraguay and Uruguay) liberalized trade among them and extended the liberalization to other members, but they had achieved a level of efficiency, maturity and specialization before hand (before liberalization) that allowed them to capitalize on this liberalization. When and at what level of development one starts the liberalization process? When and at what stage and threshold of development will the dynamic processes governing a country's growth kick in? And at what stage would self-reinforcing forces count more in shaping development, growth, benefits from trade, etc. than static efficiency conditions? There are no clear cut answers to these questions but increasingly, economists are sceptical about the undue emphasis some put on static market conditions and their neglect of the importance of dynamic forces in determining success in world markets.

One of the most distinctive features of the EEC has been the dynamic gains from internal trade liberalization. With it came rapid and extensive intra-industry trade where industries specialized in well defined niches and increased trade within the same industry. Thus, European economic integration was built on specialization within industries rather than on movement of resources from import competing to export industries. (Sapir, 1992). The key to their success was trade creation that superseded trade diversion (not that this was not important and substantial) impulses and the freeing of the mobility of resources. What started as a simple sectoral agreement in coal and steel was expanded into a free trade area with a common tariff against the rest of te world, then a common market where factors of production moved freely from one country to the other and they are steadily but slowly moving to full economic integration and harmonization of currencies, fiscal and monetary policies.

There are many lessons to learn from their experience. First, they began with sectoral agreements among a small subset of countries. Second, they moved very quickly to liberalize trade among themselves and to free the mobility of resources. Third, they gradually expanded the geographical and industrial scope of the agreement. Fourth, they erected an elaborate institutional structure to promote and cushion the adjustment processes of harmonization. Fifth, the initial interest of the United States in the success of the union (common market) was instrumental in protecting the fledgling organization through its formative years. Sixth, the intersection of the political interests of the two principal members (Germany and France) in the success of the project coupled economic interest with a strong political will to succeed.

The NAFTA agreement is a less ambitious project than the EEC. The United States aimed at enhancing its competitive position in world trade by extending its resource base to include resource rich Canada and energy rich Mexico and by associating its high cost industries with low-cost supplies from Mexico (Deardorf and Stern, 1992). The fact that there are mounting US concerns about many illegal Mexicans in the southern US states, played a major role in prompting the US to woe Mexico into its FTA with Canada. There are many problems, however, with NAFTA. It does not have any compensation mechanism to smooth the adjustment process which is borne unevenly by Mexico and Canada. It proceeded quickly with little preparation time especially for Mexico. Canada had an Auto Pact with the US since 1965, about 15 years before FTA between them came about. The jury is still out on

NAFTA's success, there are many complications that are difficult to disentangle to assess the impacts of NAFTA in isolation of the other forces. Ironically, it is the experience of NAFTA that is most relevant to the evaluation of the proposed regional arrangements for the Middle East. This follows from the fact that a developing country like Mexico is joining two more economically advanced countries.

The Asia Pacific arrangements have also some strong relevance to this issue as they involve some clear sharing and patterns of industrial deployment among the constituent members. The ASEAN and other Asia-Pacific regional economic projects are far less formal than either EEC or even NAFTA. Yamazawa (1992) argued that East Asia has not been particularly enthusiastic about formal economic integration of the EEC type. There is nothing like a Rome Treaty or a free trade area. The main mechanism underlying their cooperation is the deliberate transfer of manufacturing industry from early starters to late comers, from Japan to the NICs of Asia and from the Asian NICs to ASEAN countries. This pattern has been dubbed as the "flying geese pattern" in industrial development.

By way of summary, the lessons drawn from the experiences of several regional economic cooperation projects world wide are clear and profound. PTA's work best when they proceed slowly and cumulatively, preferably with sectoral arrangements preceding overall agreements and among a symmetrical grouping of countries that can expand their membership, when trade creation objectives go hand in hand with trade diversion, when they establish compensation mechanisms to smooth the adjustment processes in the weaker economies, when they arise out of a free democratic process and with wide participation of the population, when efficiency considerations do not subordinate equity considerations as membership is likely to expand and the durability of regional groupings is likely to be extended and solidified when member countries feel that they are treated fairly and equally, when investment liberalization forms an important plank of trade liberalization, when there are chances for redeployment of industry and for wide range intra-industry trade and specialization, when external forces are accommodating and when a principal member(s) has a strong political commitment for its success.

8.0 The New Middle East

Suppose you are in Europe in 1940 imagining the Europe of 1970, or a Japanese in 1940 imagining the Japan of 1970- How far would you dare imagine? Asked the Association for Peace of Tel Aviv (1970). Implicitly it was asking why cannot the people of the Middle East resolve their conflicts in the same way the Europeans and the Japanese did? Why cannot the frontiers of the national states of the area be open for trade and why should not cooperation replace conflict? Why should the conflicts in the Middle East today be assumed to be more important than the conflicts among Europeans a few decades ago? Peres New Middle East (1994) raises the same questions. Put in this framework, the Middle East conflict is reduced to a conflict over frontiers and a simple power struggle among neighbours. Israel is assumed to be as Middle Eastern as Germany is European and peace is touted to hold promising benefits for the Palestinians in particular and for the Arabs in general.

The enormous "Arab peace dividends" are presumed to derive from an increase in external aid, from the rebuilding of indigenous institutional capacities to guide economic and reconstruction efforts, from greater and more guaranteed access to the Israeli market and possibly other western markets with which Israel has already concluded free trade arrangements (the United States, EU and most recently

(July, 1996) Canada), from an increased Palestinian command over domestic natural resources, from the expected increase in international tourism in the region, from the decrease in military spending and from the reduction in political instability and general uncertainty that militated in the past against foreign investment in the region. The Israeli benefits are less discussed, but these, I fear, are far more important and certain than Arab benefits. In bargaining situations such as the one we are considering, relative benefits are what count. A balanced evaluation of the "dividends of peace" calls for an assessment of both sides of the ledger of peace.

The alleged gains rest on some strong claims; they have to be examined and evaluated against the background and experience of the Palestinians under occupation and against traditional economic analysis of evaluating opportunity costs and alternatives. I hasten to say that this calculus of peace is not only of interest to the Palestinians; it is also the concern of all the neighbouring Arab countries who are watching closely and carefully the events. What is unfolding in the Occupied Territories is taken as a test case and as a precedent of what is likely to await the Arab economy at large. The more realistic, credible and visible the "benefits" of peace are, the less skeptical the neighbours will be and vice versa.

The economic conditions and problems the Palestinians endured under occupation provides a background and a yardstick for judging the promises and achievements of peace and the new regional plans. Israeli occupation of the West Bank and Gaza was very costly for the Palestinians and the Arabs. These costs manifested themselves in the loss of control over water, in the loss of prime agricultural land, in the severance from traditional markets, in the constrained and limited industrial growth, in the disarticulated and precarious education, in the inadequate and insufficient investment in physical infrastructure, in the loss of the indigenous public sector that could have protected and guided the process of development, in the subjugation of the Palestinian population to the occupiers' tax and import regimes, in the transfer of the Palestinian social surplus to Israel through taxation in excess of expenditures in the territories and through scooping of the Palestinian holdings of foreign exchange, in the export of the local producers to either Israel or the Gulf, and in the destructive effects of political disruption and violence as people rebelled against the humiliating tyranny of their oppressors.

While the occupation may not be a strictly zero-sum game, Israel derived enormous gains from it. These gains included tapping freely into Palestinian water, exploiting a captive export market, drawing on cheap labour whose income was spent primarily on Israeli products, confiscating prime agricultural land and skimming all the free rents derived from it, collecting tax revenues far in excess of the occupation and its administration costs, and scooping the large foreign exchange flows from Palestinian remittances from the Gulf and elsewhere.

It is natural to expect that under peace most of these negative factors will be eliminated, some positive gains will be realized and the Palestinians would be compensated for their losses and/or suffering. Strangely, little mention of these enormous losses seem to surface when the economics of peace is discussed.

Under occupation the West Bank and Gaza were forced into an economic union with Israel, not much different from the vision of the New Middle East . A small, fragmented, disarticulated, poor and labour intensive economy was confronted with a relatively rich, advanced, capital intensive, strategic and highly centralized economy. This confrontation took place at a time when the Palestinians were denied their most vital resource (water), when access to the Israeli market was blocked and were severed from their traditional Arab markets. It is small wonder that agriculture the mainstay of the preoccupation economy and the largest employer of people faltered.

Displaced from agriculture with no alternative employment in industry, labour from the territories moved to work in Israel generally at higher pay than in the territories but at the lowest end of the Israeli wage scale. Although Palestinian workers represented no more than 7% of total employment in Israel, they constituted the majority of workers in construction and a large share of agriculture labour. On the other hand, they represented over a third of all the employed residents of the Occupied Territories. Their earnings were about one-quarter of the GNP of the West Bank and 40% of Gaza's. This export of labour and the rise in labour costs in the Occupied Territories destroyed the possibility of developing domestic manufacturing production. Earnings in Israeli Sheckels went ultimately to buy Israeli goods. Israeli net exports to the territories were over $500 million per year before the Intifada.

Israeli manufacturing could have taken advantage of cheap, unemployed and uprooted labour by locating in the territories. This did not happen. Some limited subcontracting of clothing and textile subactivities occurred, but their magnitudes were limited and were restricted to a limited subset of minor tasks generally performed by women. Some have argued that the security situation in the Occupied Territories and the general uncertainty about the future of the areas scared investment away. The Territories were under the tight grip of the IDF for so long and no meaningful investment was undertaken there. The insecurity during the Intifada and the uncertainty about the future fate of the Territories may explain the lack of investment in the late 1980's, but what about the lack of investment between 1967 and 1987?

The communal pauperization of the Palestinians by denying them access to their resources (water and land) and ultimately labour cannot be dismissed as a pure accident of history or as an unintended and incidental effect of the occupation. Rather, it is part of a long standing Israeli denial of the existence of the Palestinian as a people and a community capable of leading an independent national existence. Improvement in the economic prospects of the Palestinians then requires their reconstitution as an independent national community. No amount of international aid can make up for the loss of land and water. In a primarily agrarian economy, water is the most critical economic factor upon which the Palestinian economy can be reconstructed, at least in the initial stages of reconstitution of the economy and society.

The financial requirements for development and reconstruction of the Palestinian economy are finite but massive. The list of urgent needs for sewers, roads, schools, hospitals, ports, airports, etc. is long and dire. But finance without real resources will perpetuate the state of dependency of The Palestinian economy on outside help and on the Israeli economy. Any large investments made now will go through the Israeli economy and would most likely not be sustainable. I come to this pessimistic view from reviewing the fate of the Arab economy in the 1980's where its GDP rate of growth fell far below other regions including the Sub-Saharan Africa.

While the need for external sources of finance is urgent, the Palestinians must balance this urgency for finance against the negative and disastrous dependency on precarious international charity. They simply do not need to repeat the Arab experience in the 1970's and 1980's, and should try to avoid contacting this crippling Arab disease.

While water issues are still to be negotiated, all the Agreements concluded so far do not augur for a reasonable Palestinian control over this vital resource. There is a lot of discussion about "unitizing" the management of this "common" resource. Indeed, there are efficiencies in managing jointly this resource, but before any joint management procedures are put in place, it is critical that "property rights" over this resource be established. Agreement (OSLO I) after Agreement (Paris Protocol and OSLO II) still treat Palestinian water as Israeli charity to the Palestinians. Israel raises the share of the Palestinians by a modest amount. This presupposes Israeli exclusive control and management of water. Peace will be credible and visible to the extent the Palestinian are able to reclaim their lost land and water. Even under Oslo II and in the last third phase of the Agreement, the Palestinians will have authority over only one third of their land and less than one fifth of their water.

Dismantling the occupation should allow the Palestinians to manage their economic affairs as they choose and to protect and guide their economy in the manner they see best serve their interests. The Paris Protocol makes sure that this shall not be the case. The Palestinian economy is put under the Israeli import and tax regimes. Israel fearing that the Palestinian economy may be used to smuggle duty free goods (or act as a tax haven) into Israel moved very quickly to impose its own tariff regime (the same tariffs on all foreign goods in both Palestine authority territory and Israel). Few exceptions are allowed as an after thought to allow some latitude for the Palestinians over goods imported from countries that do not trade with Israel. The rule is the Palestinians must impose the same tariffs on imports as the Israelis. These tariffs have evolved to protect and promote the Israeli economy, they are not consistent with the interest of a fledgling economy with limited productive capacity. The Palestinians got a promise for smoother access to the Israeli market. But for now quotas are imposed on Palestinian poultry, eggs, potatoes, cucumbers, tomatoes and melons entering the Israeli market. Although the quotas, in principle, apply to exports from either side to the other, with the exception of melons these restrictions apply only to the Palestinians. The price of these Protocols is greater integration with the Israeli economy. What the Palestinians have worked out is a sort of a mix between a "Custom Union" and a "Common Market" with the Israelis. Any such arrangement generally involves "trade creation" and "trade diversion". One wonders whether giving the Israelis full and unimpeded access to the Palestinian market is good for their long term prospects in building a diversified and productive economy. For all practical purposes, this Agreement perpetuates and legitimates the economic structures that emerged under occupation. Accepting the "Trade Diversion" implications of the Agreement simply means that Palestinian Authority has preferred to tie its economic fortune to Israel rather than the Arabs. I wonder whether the Palestinian negotiators concluding this Agreement have thought carefully through all of its implications. I suspect not. It does not appear to be consistent with their interest in accessing the wider and less competitive Arab markets.

Defenders of the Agreement often quote the many advantages that economic theory generally predict to follow from freer trade in its support. The general economic belief is that smaller and poorer countries are supposed to win most from access to the market of richer partners. What is missing from this argument are many factors and conditions upon which the theory is built. Economists tend to exaggerate the spread effects of free trade and under represent its "backwash effects" and adjustment costs.

Actually, bargaining theory is perhaps clearer and more realistic about the outcomes of bargaining among unequal partners. It predicts that the party with most options is likely to dictate its interests on the party with little or no options. It does not stretch the imagination much to suggest that all the Agreements concluded so far between the Israelis and Palestinians have been concluded between unequal partners and under duress and that little else but lopsided advantages to the Israelis could have been expected from them. We are told that the gains will be from the dynamics of foreign investment, large tourism flows and higher productivity that springs from competing with more advanced competitors. But it is precisely in these areas that the Arabs will lose most.

There is the expectation that foreign investment will be attracted to the region and that peace will encourage a larger flow and a more certain attraction. That indeed is likely to be the case. But much, if not all, of this investment will likely go to the Israelis. Much of the foreign investment that is taking place today is of the Tariff-Jumping kind. The more custom unions the Israelis succeed in drawing in the region and the more clauses they eliminate from the Arab Boycott, the more foreign investment will come to them.

The Arab Boycott was very costly for the Israelis. Some estimates put the cost at $40 billion over the past four decades. I tend to believe that this cost may have been even higher. If one were to include in the estimate the amount of foreign investment that Israel could have attracted in its absence and if one were to adopt a real present value approach.

The Israelis have increasingly become concerned about the nature of their dependence on foreign aid from the United States. As pressures mount to balance the US monumental federal budget, foreign aid will most likely be at the top of the chopping agenda. Israel currently claims the lion's share of this budget, its share will sooner or later be at the chopping block. Peace will give Israel a breathing space only. It will postpone the cutting but not the cut. Foreign investment of the order of $3-4 billion will be the only reliable alternative. Israel was not very successful in attracting foreign investment in the past ($200-300 Million per year on average). With no Arab Boycott and few custom unions ensuring an unimpeded access to several Arab markets would change the picture dramatically. It is already changing. Lat year Israel was successful in raising over $1.7 billion in foreign investment. Motorola, Volks Wagon, Cable and Wireless, Intel and many other high-tech firms have plans to locate in Israel. And Israel's gain here could easily be the Arab's loss.

Foreign investment in the Arab region has drastically declined from the high levels in the 1950's. Actually the share of the region in total world foreign investment is now less than 3%. Access to world markets, new technology, advanced management systems and large investments are almost the exclusive preserve of multinationals. The Palestinians will be ill advised not to take advantage of the current favourable international climate to host and attract foreign investment.

There are abundant examples, however, of multinationals that exploit the local market, wrestle substantial concessions that far outweigh their positive contributions and provide little or no transfer of technology. It is invariably the case that positive net benefits from foreign investment were derived by enlightened governments that obstinately negotiated favourable terms from these multinationals that included product mandates, home base operations and systematic transfer of technology. In the absence of a representative and free national government and a wider Arab cooperation, the Palestinians are in a weak position to negotiate favourable terms. Besides, their chances of getting a respectable share of foreign investment could depend critically on their guaranteed access to the wider Arab market. The more the Palestinians tie their economic fortunes to the Israelis, the less likely that they will be able to derive concessions from their Arab bretherns in this regard.

Greece which is an hour flying time from Palestine attracts 12 million international tourists a year. Alternatively, Israel attracts no more than 2 million. With peace, international tourism is likely to increase rapidly. The Arab region is not well prepared for this influx. Arab tourism infrastructure is limited and international linkages are almost absent. Lebanon used to have a competitive tourism infrastructure but that was destroyed in the civil war. Today it is not even sufficient to meet the demand of returning Lebanese visitors. Egypt is the only Arab country with the capacity to benefit from the increased flow, but its share of the total is not certain.

The bottom line of tourism is length of stay. The longer tourists stay in a country the more they spend and the larger the benefits from tourism to the host country. Under the prevailing circumstances, even under peace, without sufficient planning and preparation, the rewards of of this tourism bonanza will be lost by the Arabs and may even lose existing tourism as Israel may succeed in diverting Arab tourists away from traditional Arab tourist centres (tourists from Gulf states may visit Israel instead of Lebanon or Egypt.)

The potential rewards from increased tourism are there. They would be more certain with proactive preparation and planning. A concerted Arab tourism strategy is required to mount joint marketing and advertising campaigns and to connect tourism flows. In the absence of this pro-active planning and Arab coordination, Israel will get the tourists and would determine how long, how much and where do they spend their tourist dollars. The Arabs will get at most day trippers or safari like visits where foreign tourists will simply pass by Arab areas. Most tourists will come to Israel and will make occasional short forays into Arab land. The Jordanians are already experiencing some of these negative effects.

For every dollar spent on education in the Arab world $166 is spent on defence. There is the potential prospect that if peace were to be just and enduring, there could be substantial savings in military wasteful expenditures. The Middle East has the dubious distinction of having the highest military expenditures shares in GDP than any other region in the world. Out of the ten largest spenders on the military, 7 countries are in the Middle East. Israel has already reduced her defence expenditures as a percentage of GDP from 22% of GNP before Camp David Agreement to 10% now. Israel will benefit far more than the Arabs from reallocation of resources away from the military given the high differential average productivity of the resources in the military in Israel and in the Arab world.

Israeli exports correspond very closely to Arab imports. My own calculation of the CONCORDANCE INDICES (indices of structural similarity of trade composition by commodity) show that the degree of Israeli concordance with Saudi, Iraqi, Syrian, etc trade is twice as large than the corresponding indices with Europe or the US. My estimates suggest doubling of Israeli exports under peace. Geographical proximity is another advantage for Israel in the region. Using the Palestinians as her marketing agents and door way to Arab markets can speed and raise the potential.

Israel has already gained from another trade angle that even the discussion of peace with the Palestinians brought about. In the past two years Israel had a booming trade surplus while Europe and the US were facing economic difficulties. The reason is increased trade with China, India and Japan; countries that would not have dared to do business with Israel if the new arrangements with the Palestinians were not in place.

9.0 Conclusions

The gist of the arguments here is that Israeli "peace dividends" are massive and real while Palestinian and Arab gains are conditional, precarious and highly illusive. Even when these gains are positive they are pale in comparison with those derived or to be derived by the Israelis. The peace Agreements concluded so far guarantee Israel the economic benefits it derived under occupation, open new trade vistas, allow for the reduction of defence expenditures, dismantle the Arab boycott, attract new foreign investment and new international tourism.

There is no level playing field between the Palestinians or the Arabs and the Israelis. The Agreements reflect the vertical organization of power and options in existence. What is concluded under duress cannot last. The interest of peace calls for an immediate and unconditional independence of the Palestinians and an Arab cooperation first strategy. It is only then that they can be expected to conclude meaningful, symmetrical and lasting agreements. The Arabs who are watching both the Israelis and the Palestinians are not encouraged or impressed with what they see. Israel is using its superior bargaining power to wrestle enrmous concessions from the Palestinians and now from the Jordanians. This is to be expected from independent and disjointed bargaining. Unfortunately, the only way to correct the situation will be to start all over. This is admittedly difficult. But the Arabs must make the painful economic adjustments and true "reforms" that their dependence on oil have allowed them to postpone before they contemplate joining any regional arrangement with more advanced economies. First among the pressing needs is the formation of more meaningful regional economic groupings among the Arabs that can create true dynamic gains in productivity and export performance. Once they succeed in restructuring and re-balancing their economies they will be ready for joining the world wide movement towards trade and investment liberalization.

[1] P. Kennedy, *Preparing for the Twenty-First Century* (New York: Harper Collins Publishers Ltd, 1994). p. 209.

[2] See the detailed account of these losses in Atif Kubursi. "An Economic Assessment of Total Palestinian Losses" in Sami Hadawi (1988). Palestinian Rights and Losses in 1948. (london: Saqi Books) PP. 115-189.

[3] Efraim Kleiman (February, 1995) "The Economic Provisions of the Agreement Between Israel and the PLO" The Hebrew University of Jerusalem. working Paper #300.

[4] The protocol is formally "Protocol on Economic Relations Between Israel and the PLO as Representing the Palestinian People". It is incorporated as Annex IV in the Cairo Agreement signed on May 4, 1994.

[5] See my book on The Economic Consequences of The Camp David Accords (Beirut: Institute for Palestine Studies, 1980).